

OTHER FINANCIAL INCENTIVES

Federal Tax Incentives

Income-producing properties listed on the National Register of Historic Places and/or deemed contributing to a National Register of Historic Places historic district are eligible for a tax credit based on the costs of rehabilitation. The tax credit is a dollar-for-dollar credit and not a deduction. This amount is equal to 20% of the cost of rehabilitating a property that is either listed or eligible for listing on the National Register of Historic Places. Properties that are not eligible for listing but are over 50 years of age may be eligible for a 10% tax credit. Rehabilitation must follow certain guidelines established by the National Park Service and explained in the Secretary of the Interior's Standards for Rehabilitation.

Low-Income Housing Credits

The Tax Reform Act of 1986 provides for special relief for investors in certain low-income housing projects of historic buildings. A 70% federal income tax credit is available for rehabilitation of low-income housing. If the project is federally subsidized, a 30% tax credit is available instead.

Private and Voluntary Preservation Tools

Easements

Because of federal tax considerations, the charitable gift of a preservation easement is by far the most commonly used voluntary preservation technique. A preservation easement is a formal agreement between a property owner ("grantor") and a government agency or a preservation organization ("grantee"). The easement is usually placed with the a non-profit organization that maintains the right of review and approve proposed alterations to the structure or its setting before they are undertaken, and to enforce the easement terms in event of a violation. Tax advantages are available for some easements. Federal law permits, for example, the donation of a facade easement for the purpose of preserving the exterior integrity of a qualified historic building.

Mutual Covenants

Mutual Covenants are agreements among adjacent property owners to subject each participating property owner's land to a common system of property maintenance and regulation. Such control is critical in historic areas that involve substantial amounts of open space where development of the land would irreversibly damage the historic character of an area.

Revolving Fund

A revolving fund, normally administered by a non-profit or governmental unit, establishes a monetary set value of budgeted funds dedicated for the sole purpose on which property can be bought, improved, maintained, and sold. The revolving fund is a pool of capital created and reserved for a specific activity (such as the purchase of an endangered historic building) with the condition that the money will be returned for

additional activities. Monies are subsequently returned and reused. Revolving funds have proven to be an effective tool to stimulate preservation of historic properties, both through acquisition and resale of properties, and through loans to individuals for restoration or rehabilitation. Funds are replenished through proceeds from sales, rentals, loan repayments, and interest, and revolved to new projects.

Funding to create a revolving fund is available through the National Trust for Historic Preservation. This fund provides below-market-rate loans of up to \$150,000 to nonprofit organizations and public agencies to help preserve properties listed in or eligible for the National Register of Historic Places. Funds may be used to create local revolving funds, for site acquisition or rehabilitation work. Staff recommends the City not pursue this type of revolving fund program.

Revolving Loan Funds: Low Interest Loans

The creation of a City revolving loan fund or grant program was investigated and determined to be financially infeasible. A loan fund or grant program was quickly discarded since a City managed program of this type would most likely require the use of public funds for private uses or involve substantial fundraising efforts by the City. Although this type of funding mechanism would be an ideal preservation funding tool and could support Santa Barbara's historic property owners seeking low interest financing funds for preservation or rehabilitation projects, there are also funding and management questions associated with this option.

Revolving loan funds often start small with both programmatic financing and administrative money. Project development funding, or "seed money," needs to be budgeted, donated or acquired to ensure a strong beginning for a new revolving loan fund. Over time, more and more complex deals become possible, and as success builds, the fund attracts more donations and or replenishes itself with the repayment of loans.

A variety of public or private entities can operate a revolving loan fund, but nearly all are managed by private, nonprofit organizations. Nonprofits can act more independently than government agencies, and also can take greater risks. Managing the fund, however, requires professional expertise and a great deal of time. Consequently, a separate organization may need to be established with real estate and financial services staff. For the above stated reasons, Staff recommends the City not pursue this type of financial incentive loan or grant program.

Purchase of Development Rights (PDR)

This device involves the acquisition by a local governmental agency of the right to further develop a historic property. After the acquisition of development rights, the land remains in private ownership, but the landowner has sold the right to further develop the property. By acquiring only the development rights, rather than the full-fee interest, the local government ensures that the parcel will remain in its present use, without the expense of outright purchase. Rather than paying market value for

the parcel, the community only pays the difference in the full market value of the parcel and its value in its present use. Because it remains in private ownership, the community avoids maintenance and management responsibilities. Also, the land remains on the tax rolls, albeit at a reduced valuation to reflect the land's market value in light of the development restrictions. Purchase of development rights provide permanent protection, while zoning is subject to political pressures for change. These programs typically rely on loyal bond issues or real estate transfer taxes for funding. Due to the costs associated with obtaining these development rights, Staff recommends the City not pursue this type of PDR program.

Transfer of Development Rights (TDR)

The City of Santa Barbara has a Transfer of Existing Development Rights (TEDR) Program which could be modified to allow its use for historic properties. Transfer of development rights are similar to PDRs in that the right to further develop a property is sold in order to keep the historic property at its present density. However, instead of governmental agency purchasing the rights, the landowner sells the rights to further develop the property to another private entity. The private entity in turn can then develop their own parcel of land at a density increase, beyond their zoning limits. The historic property remains in the ownership of the original owner and keeps the property on the tax rolls at a reduced rate. It simply eliminates the pressure to further develop the land. TEDR programs can achieve the same result as PDRs while avoiding the large public acquisition costs. With TEDRs, new development absorbs the cost of protecting the historic resources.

In densely developed urban areas, historic buildings can be threatened by economic forces. The demolition of a historic structure allows a property to be redeveloped to its "highest and best use." Owners of these properties may feel limited by historic designation, which can prohibit them from realizing potential higher profits from their property. A "Transfer of Development Rights" provision, if established by a city, can help rectify this financial inequity.

A Transfer of Development Rights (TDR) program allows owners of buildings in zoning districts where more intense development is permitted to sell that development potential to owners of other sites. As shown in the diagram below, air rights are literally purchased by another owner for use on a second site.

The city of Philadelphia provides an example of a Transfer of Existing Development Rights program. The TEDR program came about when an ordinance was passed to prevent the demolition of a landmark downtown building. At the same time an old "gentlemen's agreement" was broken not to build a downtown building higher than the hat on the sculpture of William Penn on the City Hall. It was recognized that development should be encouraged while the historic character of the downtown district was preserved. The Philadelphia TEDR program allowed for this, and had three goals when it was established in 1991;

- To provide an economic incentive for rehabilitation to locally designated landmarks;

- To protect the 1984 local historic preservation ordinance from court challenge by offering relief to city-certified property owners on land zoned for more profitable use;
- And to establish a new and innovative incentive for nonprofit owners of historic properties to maintain and rehabilitate their buildings.

More than 200 owners of historic structures were eligible to sell development rights through the TEDR option. This incentive was combined with two other development programs--an enhanced tax abatement program that included historic properties, and a large revolving loan fund.

The City of San Francisco has considered the use of a TEDR program as a way to encourage preservation, described in Planning Document titled "A Preservation Strategy for Downtown San Francisco." Although this type of program could achieve some additional historic protection for certain structures. Staff believes that designated historic structures already have a sufficient review process that limits on how additions can be made to these types of buildings. Staff believes this program is not necessary and recommends the City not pursue this type of TEDR program.